

<i>At or for the Years Ended December 31,</i> <b>1999</b>	1998	1997	1996	1995	
<i>(In thousands, except per share data)</i>					
<b>STATEMENT OF EARNINGS DATA:</b>					
Net sales	\$3,083,264	2,744,620	2,429,085	2,239,471	2,041,865
Cost of sales	2,306,405	2,063,333	1,869,221	1,726,765	1,594,050
Gross profit	776,859	681,287	559,864	512,706	447,815
Selling, general and administrative expenses	482,062	432,191	383,523	367,251	348,278
Restructuring costs <sup>(a)</sup>	—	—	—	700	8,439
Carrying value reduction of property, plant and equipment and other assets <sup>(b)</sup>	—	2,900	5,500	3,060	23,711
Compensation expense for stock option exercises <sup>(c)</sup>	—	—	2,600	—	4,000
Operating income	294,797	246,196	168,241	141,695	63,387
Interest expense	32,632	31,023	36,474	39,772	42,398
Acquisition costs—World Merger <sup>(d)</sup>	—	17,700	—	—	—
Other expense, net	2,266	2,667	338	4,586	1,170
	34,898	51,390	36,812	44,358	43,568
Earnings before income taxes	259,899	194,806	131,429	97,337	19,819
Income taxes	102,660	79,552	51,866	40,395	8,022
Net earnings	\$ 157,239	115,254	79,563	56,942	11,797
Basic earnings per share <sup>(e)</sup>	\$ 2.63	1.91	1.33	0.96	0.21
Weighted-average common shares outstanding <sup>(e)</sup>	59,730	60,393	59,962	59,310	57,235
Diluted earnings per share <sup>(e)</sup>	\$ 2.61	1.89	1.32	0.95	0.20
Weighted-average common and dilutive potential common shares outstanding <sup>(e)</sup>	60,349	61,134	60,453	59,899	58,485
<b>BALANCE SHEET DATA:</b>					
Working capital	\$ 560,057	438,474	389,378	390,889	305,370
Total assets	1,682,873	1,405,486	1,233,361	1,226,959	1,110,438
Short-term note payable	—	—	—	21,200	50,000
Long-term debt (including current portion)	596,065	377,089	402,854	486,952	435,940
Stockholders' equity	692,546	611,059	493,841	409,616	343,452

(a) During 1995 and 1996, the Company recorded pre-tax restructuring costs of \$8.4 million and \$0.7 million, respectively, related to certain mill closings whose operations have been consolidated into other Mohawk facilities.

(b) During 1995, the Company adopted EAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of, as of January 1, 1995. A charge of \$23.7 million was recorded for the reduction of the carrying value of property, plant and equipment at certain mills. During 1996, the Company recorded a charge of \$3.1 million arising from the write-down of property, plant and equipment to be disposed of related to the closing of a manufacturing facility in 1996 and a revision in the estimate of fair value of certain property, plant and equipment based on current market conditions related to mill closings in 1995. During 1997, the Company recorded a charge of \$5.5 million arising from a revision in the estimated fair value of certain property, plant and equipment held for sale based on current appraisals and other market information related to a mill closing in 1995. During 1998, the Company recorded a charge of \$2.9 million for the write-down of assets to be disposed of relating to the acquisition of World.

(c) Charges of \$4.0 million and \$2.6 million were recorded in 1995 and 1997, respectively, for income tax reimbursements to be made to certain executives related to the exercise of stock options granted in 1988 and 1989 in connection with the Company's 1988 leveraged buyout.

(d) The Company recorded a one-time charge of \$17.7 million in 1998 for transaction expenses related to the World Merger.

(e) The Board of Directors declared a 3-for-2 stock split on October 23, 1997, which was paid on December 4, 1997 to holders of record on November 4, 1997. Earnings per share and weighted-average common share data have been restated to reflect the split.

## Management's Discussion and Analysis of Financial Condition and Results of Operations

### GENERAL

During the three-year period ended December 31, 1999, the Company continued to experience significant growth both internally and through acquisitions.

On July 23, 1997, the Company acquired certain assets of Diamond Rug & Carpet Mills, Inc. ("Diamond") and other assets owned by Diamond's principal stockholders for approximately \$36.0 million, which consisted of \$19.6 million in cash at closing, \$7.0 million in cash over the six-month period following closing and a \$9.4 million note payable in seven annual installments of principal plus interest at 6%. The acquisition was accounted for using the purchase method of accounting.

The Company completed its acquisitions of Newmark & James, Inc. ("Newmark") and American Weavers LLC ("American Weavers") on June 30, 1998 and August 10, 1998, respectively. Both of these acquisitions were accounted for using the purchase method of accounting. On November 12, 1998, the Company acquired all of the outstanding capital stock of World Carpets, Inc. ("World") in exchange for approximately 4.9 million shares of the Company's common stock valued at \$149.5 million, based on the closing stock price on the day the agreement was executed. The acquisition of World was accounted for using the pooling-of-interests method of accounting.

On January 29, 1999, the Company acquired certain assets of Image Industries, Inc. ("Image") for approximately \$192 million, including acquisition costs and the assumption of \$30 million of tax-exempt debt, and on March 9, 1999, the Company acquired all of the outstanding capital stock of Durkan Patterned Carpets, Inc. ("Durkan") for approximately 3.1 million shares of the Company's common stock valued at \$116.5 million based on the closing stock price the day the letter of intent was executed. The Image acquisition was accounted for using the purchase method of accounting, and the Durkan acquisition was accounted for using the pooling-of-interests method of accounting.

These acquisitions have created opportunities to enhance Mohawk's operations by (i) broadening price points, (ii) increasing vertical integration efforts, (iii) expanding distribution capabilities and (iv) facilitating entry into niche businesses, such as rugs, decorative throws and table runners.

Prior to December 31, 1999, the impact of the changeover to 2000 on computer software programs and internal operating systems was uncertain and

recent publications have suggested that February 29, 2000 may cause interruptions or system failures in computer software programs or internal operating systems. In 1999, the Company spent approximately \$0.5 million to review and upgrade its computer and business systems in its effort to make these systems Year 2000 compliant and thereby avoid any interruptions resulting from the changeover to 2000 or the occurrence of February 29, 2000. To date, the Company has not incurred any significant interruptions as a result of the changeover to 2000 and the Company is not expecting significant interruptions as a result of the occurrence of February 29, 2000.

Effective January 1, 2000, the Company changed the estimated useful lives of certain property, plant and equipment. Management believes this change more accurately reflects the actual lives of these assets and is more consistent with industry practice. The prospective change is estimated to reduce annual depreciation expense by approximately \$20.0 million in 2000. See accompanying Notes to Consolidated Financial Statements for further discussion.

### RESULTS OF OPERATIONS

#### *Year Ended December 31, 1999 as Compared with Year Ended December 31, 1998*

Net sales for the year ended December 31, 1999 were \$3,083.3 million, reflecting an increase of \$338.6 million, or approximately 12.3%, over the \$2,744.6 million reported in the year ended December 31, 1998. All major product categories achieved sales increases in 1999 as compared to 1998. The Company believes that the 1999 net sales increase was attributable to internal growth and the acquisition of Image.

Quarterly net sales and the percentage changes in net sales by quarter for 1999 versus 1998 were as follows (dollars in thousands):

	1999	1998	Change
First quarter	\$ 707,167	589,473	20.0%
Second quarter	790,617	689,488	14.7
Third quarter	809,933	718,772	12.7
Fourth quarter	775,547	746,887	3.8
Total year	<u>\$3,083,264</u>	2,744,620	12.3%

The Company's fiscal calendar reflected differences for the 1999 first quarter, with four more shipping days, when compared to 1998 and four fewer shipping days when the fourth quarter of 1999 is compared to 1998.

Gross profit for 1999 was \$776.9 million (25.2% of net sales) and represented an increase over the gross profit of \$681.3 million (24.8% of net sales) for 1998. Gross profit dollars for the current year were impacted favorably by better absorption of fixed costs through higher production volume.

Selling, general and administrative expenses for 1999 were \$482.1 million (15.6% of net sales) compared to \$432.2 million (15.7% of net sales) for 1998.

Interest expense for the current year was \$32.6 million compared to \$31.0 million in 1998. The primary factor contributing to the increase was an increase in debt levels, which was attributable to acquisitions, the stock repurchase program and capital expenditures, compared to the prior year which was offset by a decrease in the Company's weighted-average interest rate in 1999.

In the current year, income tax expense was \$102.7 million, or 39.5% of earnings before income taxes. In 1998, income tax expense was \$79.6 million, representing 40.8% of earnings before income taxes. The primary reason for the decrease in the 1999 effective income tax rate was that certain costs included in the nonrecurring pre-tax charge of \$17.7 million related to the World acquisition recorded in 1998 were not deductible for income tax purposes.

*Year Ended December 31, 1998 as Compared with Year Ended December 31, 1997*

Net sales for the year ended December 31, 1998 were \$2,744.6 million, reflecting an increase of \$315.5 million, or approximately 13%, over the \$2,429.1 million reported in the year ended December 31, 1997. All major product categories achieved sales increases in 1998 as compared to 1997. These sales increases were impacted by continued favorable industry conditions and a gain in the Company's market share, which, the Company believes, primarily resulted from continued emphasis on supporting its dealers and strong customer acceptance of new product introductions.

Quarterly net sales and the percentage changes in net sales by quarter for 1998 versus 1997 were as follows (dollars in thousands):

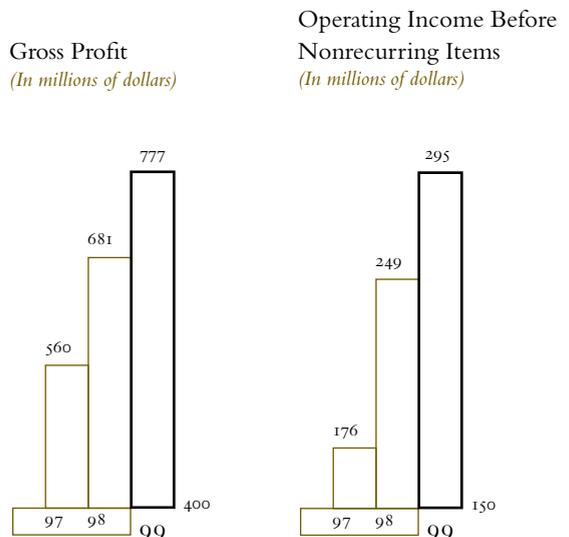
	1998	1997	Change
First quarter	\$ 589,473	537,145	9.7%
Second quarter	689,488	607,059	13.6
Third quarter	718,772	626,751	14.7
Fourth quarter	746,887	658,130	13.5
Total year	<u>\$2,744,620</u>	<u>2,429,085</u>	<u>13.0%</u>

Gross profit for 1998 was \$681.3 million (24.8% of net sales) and represented an increase over the gross profit of \$559.9 million (23.0% of net sales) for 1997. Gross profit dollars for 1998 were impacted favorably by better absorption of fixed costs through higher production volume and continued improvements in manufacturing efficiencies from restructuring efforts.

Selling, general and administrative expenses for 1998 were \$432.2 million (15.7% of net sales) compared to \$383.5 million (15.8% of net sales) for 1997. Selling, general and administrative expenses as a percentage of net sales decreased primarily due to lower administrative, bad debt and sample expenses.

During the fourth quarter of 1998, the Company recorded a charge of \$2.9 million for the write-down of fixed assets to be disposed of in connection with the World acquisition. Also, a \$17.7 million charge was recorded for nonrecurring costs associated with the World acquisition.

During the fourth quarter of 1997, the Company revised its estimate of the fair value of certain property, plant and equipment held for sale. The revision resulted in a \$5.5 million write-down to the carrying value of those assets. The revision was based upon current appraisals and other market information. In addition, a \$2.6 million charge was recorded for additional income tax reimbursements to be made to certain executives for the exercise of stock options. The income tax reimbursements were recorded in connection with stock options granted in 1988 and 1989 related to the Company's 1988 leveraged buyout.



## Management's Discussion and Analysis of Financial Condition and Results of Operations

Interest expense for 1998 was \$31.0 million compared to \$36.5 million in 1997. The primary factor contributing to the decrease was a significant reduction in debt levels.

In 1998, income tax expense was \$79.6 million, or 40.8% of earnings before income taxes. In 1997, income tax expense was \$51.9 million, representing 39.5% of earnings before income taxes. The primary reason for the increase in the 1998 effective income tax rate was that certain costs included in the nonrecurring pre-tax charge of \$17.7 million related to the World acquisition were not deductible for income tax purposes.

### LIQUIDITY AND CAPITAL RESOURCES

The Company's primary capital requirements are for working capital, capital expenditures and acquisitions. The Company's capital needs are met through a combination of internally generated funds, bank credit lines and credit terms from suppliers.

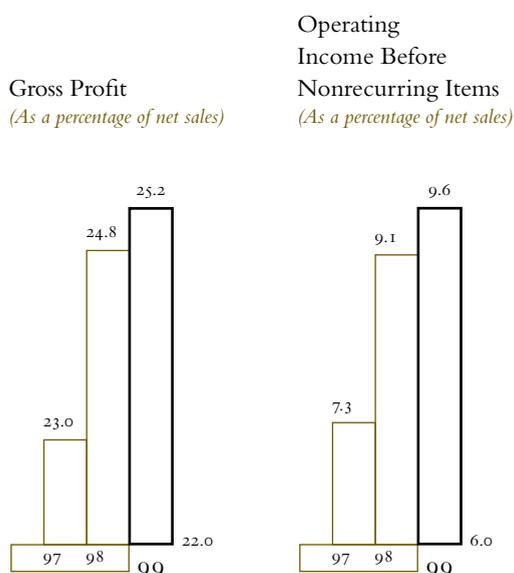
The level of accounts receivable increased from \$331.9 million at the beginning of 1999 to \$337.8 million at December 31, 1999. The \$5.9 million increase was attributable to strong sales growth. Inventories increased from \$423.8 million at the beginning of 1999 to \$494.8 million at December 31, 1999, due primarily to acquisitions and the need for a higher level of inventory to meet the increased sales volume.

Capital expenditures totaled \$146 million during 1999, and the Company spent an additional \$162 million related to the Image acquisition.

The capital expenditures made during 1999 were incurred primarily to modernize and expand manufacturing facilities and equipment. The Company's capital projects are primarily focused on increasing capacity, improving productivity and reducing costs. Capital expenditures for Mohawk, including \$233 million for acquisitions, have totaled \$510 million over the past three years. Capital spending during 2000 is expected to range from \$105 million to \$120 million, the majority of which will be used to purchase equipment to increase production capacity and productivity.

On November 23, 1999, the Company amended and restated its credit agreement to provide for an interest rate of either (i) LIBOR plus 0.2% to 0.5%, depending upon the Company's performance measured against certain financial ratios, or (ii) the prime rate less 1.0%. Additionally, the termination date of the credit agreement was extended to January 28, 2004. At December 31, 1999, the Company had credit availability of \$450 million under its revolving credit line and \$45 million under various short-term uncommitted credit lines. At December 31, 1999, a total of approximately \$110.5 million was unused under these lines. The credit agreement contains customary financial and other covenants. The Company must pay an annual facility fee ranging from .0015 to .0025 of the total credit commitment, depending upon the Company's performance measured against specific coverage ratios, under the revolving credit line.

The Company's Board of Directors approved a stock repurchase plan in September 1999, whereby the Company's management was authorized to purchase up to five million common shares. In December 1999 it amended the plan to increase the shares authorized for purchase by an additional five million shares, bringing the total authorized repurchase up to 10 million shares of its outstanding common shares. For the year ended December 31, 1999 a total of approximately four million shares of the Company's common stock had been purchased at an aggregate cost of approximately \$84 million. All this repurchase has been financed through the Company's operations and revolving line of credit.



### IMPACT OF INFLATION

Inflation affects the Company's manufacturing costs and operating expenses. The carpet industry has experienced moderate inflation in the prices of raw materials and outside processing for the last three years. The Company has generally passed along nylon fiber price increases to its customers.

**SEASONALITY**

The carpet business is seasonal, with the Company's second, third and fourth quarters typically producing higher net sales and operating income. By comparison, results for the first quarter tend to be the weakest. This seasonality is primarily attributable to consumer residential spending patterns and higher installation levels during the spring and summer months.

**CERTAIN FACTORS AFFECTING THE COMPANY'S PERFORMANCE**

In addition to the other information provided in this annual report, the following risk factors should be considered when evaluating an investment in shares of Mohawk common stock.

*A failure by Mohawk to complete acquisitions and successfully integrate acquired operations could materially and adversely affect its business.*

Management intends to pursue acquisitions of complementary businesses as part of its business and growth strategies. Although management regularly evaluates acquisition opportunities, it cannot offer assurance that it will be able to:

- successfully identify suitable acquisition candidates;
- obtain sufficient financing on acceptable terms to fund acquisitions;
- complete acquisitions;
- integrate acquired operations into Mohawk's existing operations; or
- profitably manage acquired businesses.

Acquired operations may not achieve levels of sales, operating income or productivity comparable to those of Mohawk's existing operations, or otherwise perform as expected. Acquisitions may also involve a number of special risks, some or all of which could have a material adverse effect on Mohawk's business, results of operations and financial condition, including, among others:

- possible adverse effects on Mohawk's operating results;
- diversion of Mohawk management's attention and its resources; and
- dependence on retaining and training acquired key personnel.

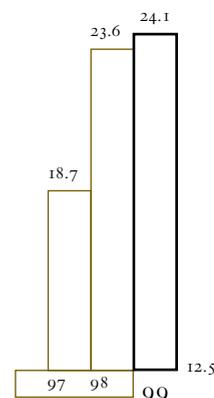
*The carpet industry is cyclical and a downturn in the overall economy could lessen the demand for Mohawk's products and impair growth and profitability.*

The carpet industry is cyclical and is influenced by a number of general economic factors. Prevailing interest rates, consumer confidence, spending for durable goods, disposable income, turnover in housing and the condition of the residential and commercial construction industries (including the number of new housing starts and the level of new commercial construction) all have an impact on Mohawk's growth and profitability. In addition, sales of Mohawk's principal products are related to construction and renovation of commercial and residential buildings. Any adverse cycle could lessen the overall demand for Mohawk's products and could, in turn, impair Mohawk's growth and profitability.

*The carpet business is seasonal and this seasonality causes Mohawk's results of operations to fluctuate on a quarterly basis.*

Mohawk is a calendar year end company and its results of operations for the first quarter tend to be the weakest. Mohawk's second, third and fourth quarters typically produce higher net sales and operating income. These results are primarily due to consumer residential spending patterns and more carpet being installed in the spring and summer months.

Return On Equity Before  
Nonrecurring Items  
*(As a percentage)*



## Management's Discussion and Analysis of Financial Condition and Results of Operations

*Mohawk's business is competitive and a failure by Mohawk to compete effectively could have a material and adverse impact on Mohawk's results of operations.* Mohawk operates in a highly competitive industry. Mohawk and other manufacturers in the carpet industry compete on the basis of price, style, quality and service. Some of Mohawk's competitors may have greater financial resources at their disposal. Mohawk has one competitor whose size could allow it certain manufacturing cost advantages compared to other industry participants. If competitors substantially increase production and marketing of competing products, then Mohawk might be required to lower its prices or spend more on product development, marketing and sales, which could adversely affect Mohawk's profitability.

*An increase in the cost of raw materials could negatively impact Mohawk's profitability.*

The cost of raw materials has a significant impact on the profitability of Mohawk. In particular, Mohawk's business requires it to purchase large volumes of nylon fiber and polypropylene resin, which is used to manufacture fiber. Mohawk does not have any long-term supply contracts for any of these products. While Mohawk generally attempts to match cost increases with price increases, large increases in the cost of such raw materials could adversely affect its business, results of operations and financial condition if it is unable to pass these costs through to its customers.

*Mohawk may be responsible for environmental cleanup, which could negatively impact profitability.*

Various federal, state and local environmental laws govern the use of Mohawk's facilities. Such laws govern:

- discharges to air and water;
- handling and disposal of solid and hazardous substances and waste; and
- remediation of contamination from releases of hazardous substances in Mohawk's facilities and off-site disposal locations.

Mohawk's operations are also governed by the laws relating to workplace safety and worker health, which, among other things, establish asbestos and noise standards and regulate the use of hazardous chemicals in the workplace. Mohawk has taken and will continue to take steps to comply with these laws. Based upon current available information, Mohawk believes that complying with environmental and safety and health requirements will

not require material capital expenditures in the foreseeable future. However, Mohawk cannot provide assurance that complying with these environmental or health and safety laws and requirements will not adversely affect its business, results of operations and financial condition. Future laws, ordinances or regulations could give rise to additional compliance or remediation costs, which could have a material adverse effect on its business, results of operations and financial condition.

### FORWARD-LOOKING INFORMATION

Certain of the matters discussed in the preceding pages, particularly regarding anticipating future financial performance, business prospects, growth and operating strategies, proposed acquisitions, new products and similar matters, and those preceded by, followed by or that otherwise include the words "believes," "expects," "anticipates," "intends," "estimates" or similar expressions constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended. For those statements, Mohawk claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve a number of risks and uncertainties. The following important factors, in addition to those discussed elsewhere in this document, affect the future results of Mohawk and could cause those results to differ materially from those expressed in the forward-looking statements: materially adverse changes in economic conditions generally in the carpet, rug and floor covering markets served by Mohawk; competition from other carpet, rug and floor covering manufacturers; raw material prices; the timing and level of capital expenditures; the successful integration of acquisitions, including the challenges inherent in diverting Mohawk management's attention and resources from other strategic matters and from operational matters for an extended period of time; the successful introduction of new products; the successful rationalization of existing operations; and other risks identified from time to time in the Company's SEC reports and public announcements.

### QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's market risk-sensitive instruments do not subject the Company to material market risk exposures.

## Consolidated Statements of Earnings

Years Ended December 31, **1999**                      1998                      1997

*(In thousands, except per share data)*

Net sales	\$3,083,264	2,744,620	2,429,085
Cost of sales	2,306,405	2,063,333	1,869,221
Gross profit	776,859	681,287	559,864
Selling, general and administrative expenses	482,062	432,191	383,523
Carrying value reduction of property, plant and equipment and other assets	—	2,900	5,500
Compensation expense for stock option exercises	—	—	2,600
Operating income	294,797	246,196	168,241
Other expense:			
Interest expense	32,632	31,023	36,474
Acquisition costs—World Merger	—	17,700	—
Other expense, net	2,266	2,667	338
	34,898	51,390	36,812
Earnings before income taxes	259,899	194,806	131,429
Income taxes	102,660	79,552	51,866
Net earnings	\$ 157,239	115,254	79,563
Basic earnings per share	\$ 2.63	1.91	1.33
Weighted-average common shares outstanding	59,730	60,393	59,962
Diluted earnings per share	\$ 2.61	1.89	1.32
Weighted-average common and dilutive potential common shares outstanding	60,349	61,134	60,453

*See accompanying notes to consolidated financial statements.*

## Consolidated Balance Sheets

December 31, **1999** | 1998

(In thousands, except per share data)

<b>ASSETS</b>		
Current assets:		
Cash	\$ —	2,384
Receivables	337,824	331,928
Inventories	494,774	423,837
Prepaid expenses	25,184	19,322
Deferred income taxes	76,628	69,464
Total current assets	934,410	846,935
Property, plant and equipment, net	624,814	454,867
Other assets	123,649	103,684
	<b>\$1,682,873</b>	<b>1,405,486</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Current portion of long-term debt	\$ 33,961	44,424
Accounts payable and accrued expenses	340,392	364,037
Total current liabilities	374,353	408,461
Deferred income taxes	53,783	47,921
Long-term debt, less current portion	562,104	332,665
Other long-term liabilities	87	5,380
Total liabilities	990,327	794,427
Stockholders' equity:		
Preferred stock, \$.01 par value; 60 shares authorized; no shares issued	—	—
Common stock, \$.01 par value; 150,000 shares authorized; 60,657 and 60,533 shares issued in 1999 and 1998, respectively	607	606
Additional paid-in capital	179,993	172,045
Retained earnings	595,932	438,408
	776,532	611,059
Less treasury stock at cost; 3,952 shares in 1999	83,986	—
Total stockholders' equity	692,546	611,059
Commitments and contingencies (Notes 10 and 12)		
	<b>\$1,682,873</b>	<b>1,405,486</b>

See accompanying notes to consolidated financial statements.

## Consolidated Statements of Stockholders' Equity

<i>(In thousands)</i>	<i>Common stock</i>		<i>Additional paid-in capital</i>	<i>Retained earnings</i>	<i>Treasury stock</i>	<i>Total stockholders' equity</i>
	<i>Shares</i>	<i>Amount</i>				
Balances at						
December 31, 1996	59,757	\$598	162,707	246,311	—	409,616
Stock options exercised	460	5	3,631	—	—	3,636
Dividends paid	—	—	—	(24)	—	(24)
Tax benefit from exercise of stock options	—	—	1,050	—	—	1,050
Net earnings	—	—	—	79,563	—	79,563
Balances at						
December 31, 1997	60,217	603	167,388	325,850	—	493,841
Stock options exercised	316	3	4,414	—	—	4,417
Dividends paid	—	—	—	(24)	—	(24)
Tax benefit from exercise of stock options	—	—	243	—	—	243
Adjustments to conform fiscal year end of World	—	—	—	(2,672)	—	(2,672)
Net earnings	—	—	—	115,254	—	115,254
Balances at						
December 31, 1998	60,533	606	172,045	438,408	—	611,059
Stock options exercised	124	1	1,390	—	—	1,391
Purchase of treasury stock	—	—	—	—	(83,986)	(83,986)
Tax benefit from exercise of stock options	—	—	836	—	—	836
Durkan pooling adjustment	—	—	5,722	—	—	5,722
Adjustments to conform fiscal year end of Durkan	—	—	—	285	—	285
Net earnings	—	—	—	157,239	—	157,239
Balances at						
December 31, 1999	60,657	\$607	179,993	595,932	(83,986)	692,546

See accompanying notes to consolidated financial statements.

## Consolidated Statements of Cash Flows

Years Ended December 31, **1999**

1998

1997

(In thousands)

Cash flows from operating activities:			
Net earnings	\$ 157,239	115,254	79,563
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation and amortization	105,297	72,591	72,893
Deferred income taxes	(1,302)	(14,194)	(3,132)
Provision for doubtful accounts	15,804	13,173	8,458
Loss (gain) on sale of property, plant and equipment	2,516	2,121	(440)
Carrying value reduction of property, plant and equipment and other assets	—	2,900	5,500
Compensation expense for stock option exercises	—	—	2,600
Changes in assets and liabilities, net of effects of acquisitions:			
Receivables	2,904	(36,523)	(33,720)
Inventories	(32,437)	(31,083)	23,610
Accounts payable and accrued expenses	(57,274)	57,295	29,953
Other assets and prepaid expenses	(16,086)	(7,653)	1,502
Other liabilities	(5,293)	(1,673)	(2,571)
Net cash provided by operating activities	171,368	172,208	184,216
Cash flows from investing activities:			
Proceeds from sale of property, plant and equipment and other assets	—	—	2,168
Additions to property, plant and equipment	(145,621)	(83,180)	(47,625)
Acquisitions	(162,463)	(36,574)	(34,141)
Other	—	—	895
Net cash used in investing activities	(308,084)	(119,754)	(78,703)
Cash flows from financing activities:			
Net change in revolving line of credit	255,530	83,658	(83,376)
Payment of note payable	—	—	(21,200)
Payments on term loans	(32,229)	(38,554)	(22,896)
Redemption of acquisition indebtedness	(20,917)	(102,201)	—
Proceeds from new loan	—	—	10,661
(Redemption) proceeds from Industrial Revenue Bonds and other, net of payments	(7,779)	11,329	11,593
Change in outstanding checks in excess of cash	15,479	(6,486)	(5,841)
Dividends paid	—	(24)	(24)
Acquisition of treasury stock	(83,986)	—	—
Common stock transactions	8,234	1,988	4,686
Net cash provided by (used in) financing activities	134,332	(50,290)	(106,397)
Net change in cash	(2,384)	2,164	(884)
Cash, beginning of year	2,384	220	1,104
Cash, end of year	\$ —	2,384	220

See accompanying notes to consolidated financial statements.

**Note I SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*(a) Basis of Presentation*

The consolidated financial statements include the accounts of Mohawk Industries, Inc. and its subsidiaries (the “Company” or “Mohawk”). All significant intercompany balances and transactions have been eliminated in consolidation. On November 12, 1998, the Company acquired all of the outstanding capital stock of World Carpets, Inc. (“World”) in exchange for 4,900 shares of the Company’s common stock (“World Merger”). On November 12, 1998, the Securities and Exchange Commission declared effective a shelf registration statement to register for resale 4,900 shares of Company common stock issued in connection with the World Merger. The historical consolidated financial statements have been restated to give retroactive effect to the World Merger. The World Merger is being accounted for as a pooling-of-interests in the accompanying consolidated financial statements.

On March 9, 1999, the Company acquired all of the capital stock of Durkan Patterned Carpets, Inc. (“Durkan”) for 3,150 shares of the Company’s common stock (“Durkan Merger”). On April 28, 1999, a shelf registration statement was filed with the Securities and Exchange Commission to register for resale 3,150 shares of the Company’s common stock in connection with the Durkan Merger. The historical consolidated financial statements have been restated to give retroactive effect to the Durkan Merger. The Durkan Merger is being accounted for as a pooling-of-interests in the accompanying consolidated financial statements.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

*(b) Accounts Receivable and Revenue Recognition*

The Company is principally a broadloom carpet and rug manufacturer and sells carpet and rugs throughout the United States principally for residential use.

The Company grants credit to customers, most of whom are retail carpet dealers, under credit terms that are customary in the industry.

Revenues are recognized when goods are shipped. The Company provides allowances for expected cash discounts, returns, claims and doubtful accounts based upon historical bad debt and claims experience and periodic evaluations of the aging of the accounts receivable.

*(c) Inventories*

Inventories are stated at the lower of cost or market (net realizable value). Cost is determined using the last-in, first-out (LIFO) method, which matches current costs with current revenues, for substantially all inventories and the first-in, first-out (FIFO) method for the remaining inventories.

*(d) Property, Plant and Equipment*

Property, plant and equipment is stated at cost, including interest on funds borrowed to finance the acquisition or construction of major capital additions. Depreciation is calculated on a straight-line basis over the estimated remaining useful lives which are 25 years for buildings and improvements and 5–7 years for furniture and equipment.

Effective January 1, 2000, the Company changed the estimated useful lives of buildings (25 years to 35 years), tufting equipment (7 years to 10 years), extrusion equipment (7 years to 15 years) and furniture and fixtures (5 years to 7 years). Management believes this change more accurately reflects the actual lives of these assets and is more consistent with industry practice. The prospective change is estimated to reduce annual depreciation expense by approximately \$20,000 in 2000.

*(e) Income Taxes*

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

## Notes to Consolidated Financial Statements

December 31, 1999, 1998 and 1997 (In thousands, except per share data)

### (f) *Earnings per Share ("EPS")*

The Company applies the provisions of Financial Accounting Standards Board ("FASB") FAS No. 128, Earnings per Share, which requires companies to present basic EPS and diluted EPS. Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company.

The Company's weighted-average common and dilutive potential common shares outstanding have been adjusted for the 3-for-2 stock split approved by the Board of Directors on October 23, 1997 and paid on December 4, 1997 to holders of record on November 4, 1997, and for the World and Durkan mergers. Dilutive common stock options are included in the diluted EPS calculation using the treasury stock method. Common stock options that were not included in the diluted EPS computation because the options' exercise price was greater than the average market price of the common shares for the periods presented are immaterial.

### (g) *Financial Instruments*

The Company's financial instruments consist primarily of cash, accounts receivable, accounts payable, notes payable and long-term debt. The carrying amount of cash, accounts receivable, accounts payable and notes payable approximates their fair value because of the short-term maturity of such instruments. Interest rates that are currently available to the Company for issuance of long-term debt with similar terms and remaining maturities are used to estimate the fair value of the Company's long-term debt. The estimated fair value of the Company's long-term debt at December 31, 1999 and 1998 was \$605,332 and \$384,242, compared to a carrying amount of \$596,065 and \$377,089, respectively.

### (h) *Fiscal Year*

The Company ends its fiscal year on December 31. Each of the first three quarters in the fiscal year ends on the Saturday nearest the calendar quarter end.

### (i) *Goodwill*

Goodwill arises in connection with business combinations accounted for as purchases. Goodwill is amortized primarily on a straight-line basis over 40 years. Amortization charged to earnings was \$2,808 in 1999, \$2,437 in 1998 and \$2,518 in 1997.

### (j) *Impairment of Long-Lived Assets*

The Company accounts for long-lived assets in accordance with the provisions of FAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of. Under FAS No. 121, the Company evaluates impairment of long-lived assets on a business unit basis, rather than on an aggregate entity basis, whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. If the sum of the expected future undiscounted cash flows is less than the carrying amount of the asset, an impairment loss is recognized. Measurement of an impairment loss for long-lived assets is based on the fair value of the asset.

### (k) *Effect of New Accounting Pronouncement*

In 1997, the FASB issued FAS No. 131, Disclosures about Segments of an Enterprise and Related Information, which supersedes FAS No. 14, Financial Reporting for Segments of a Business Enterprise. This statement, which the Company was required to adopt in fiscal year 1998, requires public companies to report certain financial and descriptive information about their reportable operating segments, including related disclosures about products and services, geographic areas and major customers. The implementation of FAS No. 131 did not have a material effect on the Company's consolidated financial statements.

### (l) *Reclassifications*

Certain prior period financial statement balances have been reclassified to conform with the current period's presentation.

December 31, 1999, 1998 and 1997 (In thousands, except per share data)

**Note 2 ACQUISITIONS**

The Company completed its acquisitions of Newmark & James, Inc. and American Weavers LLC on June 30, 1998 and August 10, 1998, respectively. Both of these acquisitions have been accounted for under the purchase method of accounting and their results are included in the Company's 1998 consolidated statement of earnings from the respective dates of acquisition.

On November 12, 1998, the Company acquired all of the outstanding capital stock of World in exchange for 4,900 shares of the Company's common stock. The acquisition of World has been accounted for under the pooling-of-interests basis of accounting and, accordingly, the Company's historical consolidated financial statements have been restated to include the accounts and results of operations of World. The Company incurred before-tax, nonrecurring charges aggregating \$20,600 in 1998 related to the World Merger, of which \$17,700 of the charge was recorded as non-operating expense and \$2,900 of the charge was recorded as a write-down of World computer equipment that was disposed of.

On January 29, 1999, the Company acquired certain assets of Image Industries, Inc. ("Image") for approximately \$192,000, including acquisition costs and the assumption of \$30,000 of tax-exempt debt. The acquisition was accounted for using the purchase method of accounting and, accordingly, the purchase price was allocated to the assets acquired and liabilities assumed based on the estimated fair values at the date of acquisition. The estimated fair values were \$205,366 for assets acquired and \$42,903 for liabilities assumed.

The operating results of Image are included in the Company's 1999 consolidated statement of earnings from the date of acquisition. The following unaudited pro forma information presents a summary of consolidated results of operations of the Company and Image for the fiscal years ended December 31, 1999 and 1998, respectively, as if the acquisition had occurred at the beginning of 1998.

	1999	1998
Net sales	\$3,099,113	2,946,736
Net earnings	\$ 156,877	119,360
Basic earnings per share	\$ 2.63	1.98
Diluted earnings per share	\$ 2.60	1.95

On March 9, 1999, the Company acquired all of the outstanding capital stock of Durkan for approximately 3,100 shares of the Company's common stock valued at \$116,500 based on the closing price the day the letter of intent was executed. The Durkan acquisition has been accounted for under the pooling-of-interests method of accounting and, accordingly, the Company's historical consolidated financial statements have been restated to include the accounts and results of operations of Durkan.

The results of operations previously reported by the separate enterprises and the combined amounts presented in the accompanying consolidated financial statements are presented below:

	Three Months Ended April 3, 1999	Year Ended December 31, 1998	Year Ended December 31, 1997
	(unaudited)		
Net sales			
Mohawk	\$683,494	2,638,820	2,327,341
Durkan	23,673	105,800	101,744
Combined	<u>\$707,167</u>	<u>2,744,620</u>	<u>2,429,085</u>
Net earnings			
Mohawk	\$ 27,128	107,613	73,424
Durkan	764	7,641	6,139
Combined	<u>\$ 27,892</u>	<u>115,254</u>	<u>79,563</u>

Prior to the combination, Durkan's fiscal year ended on February 28. In recording the pooling-of-interests combination, Durkan's financial statements for the year ended December 31, 1999 were combined with Mohawk's consolidated financial statements for the same period. Durkan's financial statements for the years ended February 27, 1999, and February 28, 1998 were combined with Mohawk's financial statements for the years ended December 31, 1998 and 1997, respectively.

## Notes to Consolidated Financial Statements

December 31, 1999, 1998 and 1997 (In thousands, except per share data)

An adjustment has been made to stockholders' equity in the year ended December 31, 1999 to eliminate the effect of including Durkan's results of operations for the two months ended February 28, 1999 in the Company's consolidated financial statements for the years ended December 31, 1999 and 1998. There were no significant intercompany transactions between Mohawk and Durkan prior to the combination.

### Note 3 RECEIVABLES

Receivables are as follows:

	1999	1998
Customers, trade	\$405,477	385,783
Other	2,826	4,378
	<u>408,303</u>	<u>390,161</u>
Less allowance for discounts, returns, claims and doubtful accounts	70,479	58,233
Net receivables	<u>\$337,824</u>	<u>331,928</u>

### Note 4 INVENTORIES

The components of inventories are as follows:

	1999	1998
Finished goods	\$254,179	219,776
Work in process	65,456	60,266
Raw materials	175,139	143,795
Total inventories	<u>\$494,774</u>	<u>423,837</u>

### Note 5 PROPERTY, PLANT AND EQUIPMENT

Following is a summary of property, plant and equipment:

	1999	1998
Land	\$ 21,767	14,320
Buildings and improvements	236,119	177,264
Machinery and equipment	791,839	613,997
Furniture and fixtures	33,436	31,666
Leasehold improvements	4,854	5,085
Construction in progress	51,645	41,576
	<u>1,139,660</u>	<u>883,908</u>
Less accumulated depreciation and amortization	514,846	429,041
Net property, plant and equipment	<u>\$ 624,814</u>	<u>454,867</u>

Property, plant and equipment includes capitalized interest of \$3,213, \$1,661 and \$799 in 1999, 1998 and 1997, respectively.

During 1998, the Company recorded a charge of \$2,900 related to a write-down of computer equipment acquired in the World acquisition and disposed of in 1999.

During 1997, the Company recorded a charge of \$5,500 arising from a revision in the estimated fair value of certain property, plant and equipment held for sale based on current appraisals and other market information related to a mill closing in 1995.

### Note 6 OTHER ASSETS

The components of other assets are summarized below:

	1999	1998
Goodwill, net of accumulated amortization of \$13,171 and \$10,363, respectively	\$113,560	85,972
Other assets	10,089	17,712
Total other assets	<u>\$123,649</u>	<u>103,684</u>

### Note 7 LONG-TERM DEBT

On November 23, 1999, the Company amended and restated its credit agreement to provide for an interest rate of either (i) LIBOR plus 0.2% to 0.5%, depending upon the Company's performance measured against certain financial ratios, or (ii) the prime rate less 1.0%. Additionally, the termination date of the credit agreement was extended to January 28, 2004. At December 31, 1999, the Company had credit availability of \$450,000 under its revolving credit line and \$45,000 under various short-term uncommitted credit lines. At December 31, 1999, a total of \$110,548 was unused under these lines. The credit agreement contains customary financial and other covenants. The Company must pay an annual facility fee ranging from .0015 to .0025 of the total credit commitment, depending upon the Company's performance measured against specific coverage ratios, under the revolving credit line.

December 31, 1999, 1998 and 1997 (In thousands, except per share data)

Long-term debt consists of the following:

	1999	1998
Revolving line of credit, due January 28, 2004	\$384,452	128,922
Durkan term loans, interest payable at prime or LIBOR plus 1.5% to 3%, payable in monthly installments of \$207	—	11,696
Durkan revolving line of credit, interest payable at LIBOR plus 1.25% to 2.75%, due November 1999	—	3,277
Note payable to Durkan officer, interest payable at 8.5%, due February 2000	—	5,400
8.46% senior notes, payable in annual principal installments beginning in 1998, due September 16, 2004, interest payable quarterly	71,429	85,714
7.14%–7.23% senior notes, payable in annual principal installments beginning in 1997, due September 1, 2005, interest payable semiannually	56,666	66,111
8.48% term loans, payable in annual principal installments, due October 26, 2002, interest payable quarterly	17,143	22,857
7.58% senior notes, payable in annual principal installments beginning in 1997, due July 30, 2003, interest payable semiannually	5,714	7,143
6% term note, payable in annual principal and interest installments beginning in 1998, due July 23, 2004	6,679	8,014
Industrial Revenue Bonds and other	53,982	37,955
Total long-term debt	596,065	377,089
Less current portion	33,961	44,424
Long-term debt, excluding current portion	<u>\$562,104</u>	<u>332,665</u>

The aggregate maturities of long-term debt as of December 31, 1999 are as follows:

2000	\$ 33,961
2001	33,593
2002	33,396
2003	27,179
2004	409,546
Thereafter	<u>58,390</u>
	<u>\$596,065</u>

**Note 8 ACCOUNTS PAYABLE AND ACCRUED EXPENSES**

Accounts payable and accrued expenses are as follows:

	1999	1998
Outstanding checks in excess of cash	\$ 42,373	26,897
Accounts payable, trade	159,812	159,966
Accrued expenses	83,253	126,023
Accrued compensation	54,954	51,151
Total accounts payable and accrued expenses	<u>\$340,392</u>	<u>364,037</u>

**Note 9 STOCK OPTIONS, STOCK COMPENSATION AND TREASURY STOCK**

Under the Company's 1992 and 1993 stock option plans, options may be granted to directors and key employees through 2002 and 2003 to purchase a maximum of 2,250 and 675 shares of common stock, respectively. During 1999, options to purchase 20 and 356 shares, respectively, were granted under these plans. Options granted under each of these plans expire 10 years from the date of grant and become exercisable at such dates and at prices as determined by the Compensation Committee of the Company's Board of Directors.

During 1996, the Company adopted the 1997 Non-Employee Director Stock Compensation Plan. The plan provides for awards of common stock of the Company for nonemployee directors to receive in lieu of cash for their annual retainers. During 1999, a total of 3 shares were awarded to the non-employee directors under the plan.

During 1997, the Board of Directors adopted the 1997 Long-Term Incentive Plan whereby the Company reserved 2,550 shares of common stock for issuance in connection with options and awards. During 1999, a total of 433 shares were awarded to employees under this plan.

## Notes to Consolidated Financial Statements

December 31, 1999, 1998 and 1997 (In thousands, except per share data)

Additional information relating to the Company's stock option plans follows:

	1999	1998	1997
Options outstanding at beginning of year	1,387	1,568	2,142
Options granted	809	174	65
Options exercised	(124)	(316)	(460)
Options canceled	(29)	(39)	(179)
Options outstanding at end of year	2,043	1,387	1,568
Options exercisable at end of year	873	686	742
Option prices per share:			
Options granted during the year	\$19.69–35.13	17.23–32.31	5.67–19.38
Options exercised during the year	\$ 5.67–19.17	5.67–19.38	0.02–19.17
Options canceled during the year	\$ 9.33–35.13	5.67–31.94	5.67–19.17
Options outstanding at end of year	\$ 5.61–35.13	5.61–32.31	5.61–19.38

A charge of \$2,600 was recorded in the fourth quarter of 1997 for income tax reimbursements to be made to certain executives for the exercise of stock options. The income tax reimbursements were recorded in connection with stock options granted in 1988 and 1989 related to the Company's 1988 leveraged buyout. The agreements allowed the Company to receive an income tax benefit on its tax return for the tax effect of the taxable compensation provided to the individuals upon the exercise of these options. Such income tax benefit resulted in a direct increase in stockholders' equity of \$7,606 in 1996 primarily from the exercise of these options.

As allowed under FAS No. 123, the Company accounts for stock options granted as prescribed

under Accounting Principles Board Opinion No. 25, which recognizes compensation cost based upon the intrinsic value of the award. Accordingly, no compensation expense has been recognized in the consolidated statement of earnings for any stock options granted in 1999, 1998 and 1997. The following table represents pro forma net income and pro forma earnings per share had the Company elected to account for stock option grants using the fair value based method.

	1999	1998	1997
Net income			
As reported	\$157,239	115,254	79,563
Pro forma	155,282	114,411	78,898
Net income per common share (basic)			
As reported	\$ 2.63	1.91	1.33
Pro forma	2.60	1.89	1.32
Net income per common share (diluted)			
As reported	\$ 2.61	1.89	1.32
Pro forma	2.57	1.87	1.31

This pro forma impact only takes into account options granted since January 1, 1996 and is likely to increase in future years as additional options are granted and amortized ratably over the vesting period. The average fair value of options granted during 1999, 1998 and 1997 was \$15.28, \$17.24 and \$9.41, respectively. This fair value was estimated using the Black-Scholes option pricing model based on a weighted-average market price at grant date of \$26.48 in 1999, \$30.44 in 1998 and \$17.03 in 1997 and the following weighed-average assumptions:

	1999	1998	1997
Dividend yield	—	—	—
Risk-free interest rate	6.4%	4.7%	6.2%
Volatility	46.7%	48.9%	45.0%
Expected life (years)	7	7	7

Summarized information about stock options outstanding and exercisable at December 31, 1999 is as follows:

Exercise Price Range	Outstanding			Exercisable	
	Number of Shares	Average Life <sup>(1)</sup>	Average Price <sup>(2)</sup>	Number of Shares	Average Price <sup>(2)</sup>
Under \$11.00	741	5.56	\$10.54	538	10.29
\$12.00 to 17.00	204	4.63	14.40	189	14.49
\$17.00 to 19.69	531	8.38	19.49	118	19.03
\$19.94 to 31.94	276	8.97	29.06	25	31.11
\$32.00 to 36.00	291	9.11	34.93	3	32.31
Total	2,043			873	

(1) Weighted-average contractual life remaining in years.

(2) Weighted-average exercise price.

December 31, 1999, 1998 and 1997 (In thousands, except per share data)

The Company's Board of Directors approved a stock repurchase plan in September 1999, whereby the Company's management was authorized to purchase up to 5,000 common shares. In December 1999 it amended the plan to increase the shares authorized for purchase by an additional 5,000 shares, bringing the total authorized repurchase up to 10,000 shares of its outstanding common shares. For the year ended December 31, 1999, a total of 3,952 shares of the Company's common stock had been purchased at an aggregate cost of \$83,986. All of this repurchase has been financed through the Company's operations and revolving line of credit.

#### Note I O EMPLOYEE BENEFIT PLANS

The Company has a 401(k) retirement savings plan (the "Plan") open to substantially all of its employees who have completed one year of eligible service. The Company contributes \$0.50 for every \$1.00 of employee contributions up to a maximum of 4% of the employee's salary. The Company amended the Plan during 1999 to match an additional \$0.25 for every \$1.00 of employee contributions in excess of 4% of the employee's salary up to a maximum of 6%. This change is effective January 1, 2000. Employee and employer contributions to the Plan were \$14,873 and \$5,080 in 1999, \$12,345 and \$4,213 in 1998, and \$9,334 and \$3,075 in 1997, respectively. The Company also made a discretionary contribution to the Plan of \$2,100 during the year.

A portion of the employees who were not eligible to participate in the Plan participated in a defined contribution profit-sharing plan through June 1997. After June 1997, the employee balances in the profit-sharing plan were rolled over into the 401(k) retirement savings plan. Contributions were discretionary and the Company expensed \$991 for the year ended December 31, 1997.

The World Carpet Savings Retirement Plan (the "World Plan"), a defined contribution 401(k) plan covering substantially all World employees, was merged into the Plan on March 1, 1999. Employees were eligible to participate upon completion of one year of service. Under the terms of the World Plan, World would match employee contributions up to a maximum of 2% of the employee's salary, and

employees vested in the contributions based on years of credited service. For the years ended December 31, 1999, 1998 and 1997, the Company contributed approximately \$142, \$703 and \$698, respectively, to the World Plan.

Durkan maintains a 401(k) retirement savings plan (the "Durkan Plan") open to substantially all Durkan employees. Durkan contributes \$0.50 for every \$1.00 of employee contributions up to a maximum of 6% of eligible wages. For the years ended December 31, 1999, 1998 and 1997, Durkan contributed approximately \$343, \$328 and \$265, respectively, to the Durkan Plan.

#### Note I I INCOME TAXES

Income tax expense attributable to earnings before income taxes for the years ended December 31, 1999, 1998 and 1997 consists of the following:

	Current	Deferred	Total
<b>1999:</b>			
U.S. federal	\$ 92,736	(1,928)	90,808
State and local	12,104	(252)	11,852
	<u>\$104,840</u>	<u>(2,180)</u>	<u>102,660</u>
<b>1998:</b>			
U.S. federal	\$ 75,985	(11,485)	64,500
State and local	17,761	(2,709)	15,052
	<u>\$ 93,746</u>	<u>(14,194)</u>	<u>79,552</u>
<b>1997:</b>			
U.S. federal	\$ 45,921	(2,540)	43,381
State and local	9,077	(592)	8,485
	<u>\$ 54,998</u>	<u>(3,132)</u>	<u>51,866</u>

Income tax expense attributable to earnings before income taxes differs from the amounts computed by applying the U.S. statutory federal income tax rate to earnings before income taxes as follows:

	1999	1998	1997
Computed "expected" tax expense	\$ 90,965	68,182	46,000
State and local income taxes, net of federal income tax benefit	7,704	9,784	4,810
Amortization of goodwill	684	746	472
Other, net	3,307	840	584
	<u>\$102,660</u>	<u>79,552</u>	<u>51,866</u>

## Notes to Consolidated Financial Statements

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The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 1999 and 1998 are presented below:

	1999	1998
Deferred tax assets:		
Accounts receivable	\$ 21,621	17,860
Inventories	15,533	12,381
Accrued expenses	41,366	39,442
Gross deferred tax assets	<u>78,520</u>	<u>69,683</u>
Deferred tax liabilities:		
Plant and equipment	(47,138)	(43,428)
Prepaid expenses	(1,892)	(219)
Other	(6,645)	(4,493)
Gross deferred tax liabilities	<u>(55,675)</u>	<u>(48,140)</u>
Net deferred tax assets	<u>\$ 22,845</u>	<u>21,543</u>

Based upon the level of historical and projected taxable income over periods in which the deferred tax assets are deductible, the Company's management believes it is more likely than not the Company will realize the benefits of these deductible differences at December 31, 1999.

### Note I 2 COMMITMENTS AND CONTINGENCIES

The Company is obligated under various capital and operating leases for office and manufacturing space, machinery and equipment.

Future minimum lease payments under non-cancelable capital and operating leases (with initial or remaining lease terms in excess of one year) at December 31, 1999 are:

	Capital Leases	Operating Leases	Total Future Payments
2000	\$2,009	30,168	32,177
2001	1,432	24,979	26,411
2002	1,223	19,926	21,149
2003	647	15,188	15,835
2004	—	10,797	10,797
Thereafter	—	20,118	20,118
Total payments	<u>\$5,311</u>	<u>121,176</u>	<u>126,487</u>
Less amount representing interest	<u>608</u>		
Present value of capitalized lease payments with a weighted interest rate of 7.85%	<u>\$4,703</u>		

The Company assumed several capitalized leases from recent acquisitions for machinery and equipment, at a cost of \$8,899 for both periods ended December 31, 1999 and 1998. The amortization of these capital leases is included in depreciation expense. Accumulated amortization was \$3,619 at December 31, 1999 and \$2,547 at December 31, 1998.

Rental expense under operating leases was \$28,407, \$27,347 and \$20,970 in 1999, 1998 and 1997, respectively.

In December 1995, the Company and four other carpet manufacturers were added as defendants in a purported class action lawsuit, *In re Carpet Antitrust Litigation*, pending in the United States District Court for the Northern District of Georgia, Rome Division. The amended complaint alleges price-fixing regarding polypropylene products in violation of Section One of the Sherman Act. In September 1997, the Court determined that the plaintiffs met their burden of establishing the requirements for class certification and granted the plaintiffs' motion to certify the class. The Company is a party to two consolidated lawsuits captioned *Gaehwiler v. Sunrise Carpet Industries, Inc. et al. and Patco Enterprises, Inc. v. Sunrise Carpet Industries, Inc. et al.*, both of which were filed in the Superior Court of the State of California, City and County of San Francisco, in 1996. Both complaints were brought on behalf of a purported class of indirect purchasers of carpet in the State of California and seek damages for alleged violations of California antitrust and unfair competition laws. The complaints filed do not specify any amount of damages but do request for any unlawful conduct to be enjoined and treble damages plus reimbursement for fees and costs. In October 1998, two plaintiffs, on behalf of an alleged class of purchasers of nylon carpet products, filed a complaint in the United States District Court for the Northern District of Georgia against the Company and two of its subsidiaries, as well as a competitor and one of its subsidiaries. The complaint alleges that the Company acted in concert with other carpet manufacturers to restrain competition in the sale of certain nylon carpet products. The Company has filed an answer, denied the allegations in the complaint and set forth its defenses. In February 1999, a similar complaint was filed in the Superior Court of the State of California, City and County of

## Notes to Consolidated Financial Statements

*December 31, 1999, 1998 and 1997 (In thousands, except per share data)*

San Francisco, on behalf of a purported class based on indirect purchases of nylon carpet in the State of California and alleges violations of California antitrust and unfair competition laws. The complaints described above do not specify any specific amount of damages but do request injunctive relief and treble damages plus reimbursement for fees and costs. The Company believes it has meritorious defenses and intends to vigorously defend against these actions.

### **Note I 3 CONSOLIDATED STATEMENTS OF CASH FLOWS INFORMATION**

Supplemental disclosures of cash flow information are as follows:

	1999	1998	1997
Net cash paid during the year for:			
Interest	\$ 37,740	30,852	37,849
Income taxes	\$120,371	75,640	55,882

### **Note I 4 QUARTERLY FINANCIAL DATA (UNAUDITED)**

The supplemental quarterly financial data are as follows:

	<i>Quarters Ended</i>	<i>April 3,</i>	<i>July 3,</i>	<i>October 2,</i>	<i>December 31,</i>
		1999	1999	1999	1999
Net sales		\$707,167	790,617	809,933	775,547
Gross profit		178,329	200,911	203,246	194,373
Net earnings		27,892	44,093	45,079	40,175
Basic earnings per share		0.46	0.73	0.74	0.70
Diluted earnings per share		0.46	0.72	0.74	0.70

	<i>Quarters Ended</i>	<i>March 28,</i>	<i>June 27,</i>	<i>September 26,</i>	<i>December 31,</i>
		1998	1998	1998	1998
Net sales		\$589,473	689,488	718,772	746,887
Gross profit		136,389	177,606	177,762	189,530
Net earnings		17,135	35,947	37,060	25,112
Basic earnings per share		0.28	0.60	0.61	0.42
Diluted earnings per share		0.28	0.59	0.61	0.41

## Independent Auditors' Report

### *The Board of Directors and Stockholders*

#### *Mohawk Industries, Inc.:*

We have audited the accompanying consolidated balance sheets of Mohawk Industries, Inc. and subsidiaries as of December 31, 1999 and 1998, and the related consolidated statements of earnings, stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 1999. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the consolidated statements of operations and cash flows of World Carpets, Inc. and Subsidiary, a wholly owned subsidiary, for the year ended June 28, 1998, which statements of operations and cash flows have been combined with those of Mohawk Industries, Inc. and subsidiaries for the year ended December 31, 1997. The consolidated statement of operations of World Carpets, Inc. and Subsidiary reflects total net sales constituting 18 percent for the year ended December 31, 1997, of the related consolidated total. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for World Carpets, Inc. and Subsidiary, is based solely on the report of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain

reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mohawk Industries, Inc. and subsidiaries as of December 31, 1999 and 1998, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1999, in conformity with generally accepted accounting principles.

**KPMG LLP**

Atlanta, Georgia  
February 11, 2000

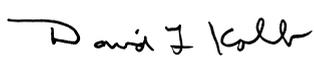
### Management's Report

The management of Mohawk Industries, Inc. is responsible for the integrity and objectivity of the consolidated financial statements. The financial statements were prepared in conformity with generally accepted accounting principles. Some of the amounts included in these consolidated financial statements are estimates based upon management's best judgment of current conditions and circumstances. Management is also responsible for preparing other financial information included in the annual report.

The Company's management depends on the Company's internal control structure to assure itself of the reliability of the financial statements. The internal control structure is designed to provide reasonable assurance, at appropriate cost, that assets are safeguarded and transactions are executed in accordance with management's authorizations and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Periodic reviews of internal controls are made by management and the internal audit function, and corrective action is taken if needed.

The Audit Committee of the Board of Directors, consisting of outside directors, provides oversight of financial reporting. The Company's internal audit function and independent auditors meet with the Audit Committee to discuss financial reporting and internal control issues and have full and free access to the Audit Committee.

The consolidated financial statements have been audited by the Company's independent auditors and their report is presented above. The independent auditors are approved each year by the Audit Committee and the Board of Directors.



David L. Kolb  
Chairman and  
Chief Executive Officer



John D. Swift  
Chief Financial Officer

**CORPORATE HEADQUARTERS**

P.O. Box 12069  
 160 South Industrial Boulevard  
 Calhoun, Georgia 30703  
 (706) 629-7721

**INDEPENDENT AUDITORS**

KPMG LLP  
 Atlanta, Georgia

**CORPORATE COUNSEL**

Alston & Bird LLP  
 Atlanta, Georgia

**TRANSFER AGENT AND REGISTRAR**

First Union National Bank  
 Corporate Trust Client Services  
 1525 West W.T. Harris Blvd.  
 Charlotte, North Carolina 28288-1153  
 (704) 590-7382

**PUBLICATIONS**

The Company's Annual Report, Proxy Statement, Form 10-K and 10-Q reports are available without charge and can be ordered via our stockholder communications service at 1-800-625-7721 or via the Internet at [www.mohawkind.com](http://www.mohawkind.com). Written requests should be sent to:

Christi Scarbro  
 Mohawk Industries, Inc.  
 P.O. Box 12069  
 160 South Industrial Boulevard  
 Calhoun, Georgia 30703

**PRODUCT INQUIRIES**

For more information about Mohawk's products, call toll-free: 1-800-622-6227.

**INVESTOR/ANALYST CONTACT**

For additional information about Mohawk, please contact:

John D. Swift  
 Chief Financial Officer  
 Mohawk Industries, Inc.  
 P.O. Box 12069  
 160 South Industrial Boulevard  
 Calhoun, Georgia 30703  
 (706) 624-2247

**ANNUAL MEETING OF STOCKHOLDERS**

The Annual Meeting of Stockholders of Mohawk Industries, Inc. will be held at the Company's headquarters on South Industrial Boulevard in Calhoun, Georgia, on Thursday, May 18, 2000 at 10:00 a.m. For directions and a map, call Christi Scarbro at (706) 624-2246.

**COMMON STOCK PRICE RANGE**

Mohawk's common stock is traded on the New York Stock Exchange under the symbol MHK. The table below sets forth the high and low sales prices per share of the common stock as reported by the exchange, for each fiscal period indicated.

**MOHAWK COMMON STOCK**

1999	High	Low
First quarter	\$42.00	25.94
Second quarter	38.56	28.19
Third quarter	30.44	18.38
Fourth quarter	26.81	19.69
1998		
First quarter	\$33.50	20.50
Second quarter	35.50	28.44
Third quarter	34.94	22.63
Fourth quarter	42.44	22.69

**COMMON STOCKHOLDERS OF RECORD**

As of February 28, 2000, there were 467 common stockholders of record.

**ENVIRONMENTAL AWARENESS**

Mohawk supports environmental awareness by encouraging recycling, waste management and energy conservation in its business practices and operating procedures.

Mohawk Industries, Inc. is an equal opportunity employer.

 Printed on recycled paper.

Mohawk Industries, Inc.

P.O. Box 12069 160 South Industrial Boulevard Calhoun, Georgia 30703 706-629-7721